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November 23, 2016

**VIA ELECTRONIC FILING**

Daniel P. Wolf  
Executive Secretary  
Minnesota Public Utilities Commission  
121 Seventh Place East, Suite 350  
St. Paul, MN 55101

Re: Additional Reply Comments of Minnesota Energy Resources Corporation

Petition of Minnesota Energy Resources Corporation for Approval of Recovery of Natural Gas Extension Project Costs through a Rider and a New Area Surcharge for the Esko Project  
Docket No. G011/M-16-655

Dear Mr. Wolf:

On November 16, 2016, the Minnesota Department of Commerce, Division of Energy Resources (the "Department") submitted Response Comments in the above-referenced docket responding to Minnesota Energy Resources Corporation's ("MERC's" or the "Company's") October 13, 2016, Reply Comments. In its Response Comments, the Department continued to support its initial recommendation that the Commission deny MERC's petition to recover Esko Project costs through a Natural Gas Extension Project ("NGEP") Rider and a New Area Surcharge ("NAS") for the Esko Project and instead approve a 30-year NAS with no NGEP Rider recovery.

MERC submits these Additional Reply Comments in response to the Department's comments and recommendations. As discussed in MERC's October 13, 2016, Comments and in greater detail below, the Department's alternative proposal is inconsistent with a workable extension project as the higher NAS would deter customer participation. If the Commission adopts the Department's recommendation and only approves the 30-year NAS, MERC would not proceed with the Esko Project and would withdraw the petition in this docket.

**1. Use of NGEP Rider in Conjunction with NAS**

With respect to MERC's proposal to utilize the NAS mechanism in combination with an NGEP Rider, the Department continues to recommend that the Commission deny MERC's request to recover Esko Project costs through both an NGEP Rider and an

NAS. In its Response Comments, the Department concludes that “the applicable statute is open to interpretation in this proceeding” and that “the Commission has the discretion to choose the recovery method that it determines is in the public interest.”<sup>1</sup> While MERC agrees with the Department that the Commission has discretion to determine whether MERC’s proposed NGEF Rider and NAS recovery are reasonable and consistent with the public interest, MERC continues to dispute the Department’s position that approval of an NGEF Rider and an NAS for the same project is somehow inappropriate or inconsistent with the law.

As discussed in MERC’s October 13, 2016, Reply Comments, the NGEF statute, Minn. Stat. § 216B.1638 (“NGEF Statute”), is unambiguous in that it does not prohibit the use of an NGEF Rider in combination with an NAS and was broadly drafted to cover a variety of circumstances, including the use of the rider in concert with the NAS mechanism in order to serve the legislative goals of enhancing natural gas service to unserved and inadequately served areas. If the legislature’s intent is clear from the statute’s plain and unambiguous language, the Commission must interpret the statute “according to its plain meaning without resorting to the canons of statutory construction.”<sup>2</sup> Nothing in the plain language of the statute limits the approval of an NGEF Rider in conjunction with an NAS. Rather, the NGEF Statute unambiguously requires that the Commission “shall approve a public utility’s petition for a rider to recover the costs of a natural gas extension project if it determines that: (1) the project is designed to extend natural gas service to an unserved or inadequately served area; and (2) project costs are reasonable and prudently incurred.”<sup>3</sup>

The Department continues to argue that the NGEF Statute’s definition of contribution in aid of construction (“CIAC”) supports a finding that the NGEF Statute was not intended to be approved in combination with an NAS because, according to the Department, the NGEF Statute’s definition of a CIAC is limited to contributions by “developer[s]” and “local government” and “does [not] include recovery from the customers in the new area.”<sup>4</sup> As discussed in MERC’s October 13, 2016, Reply Comments and contrary to the Department’s reading of the NGEF Statute, the term “developer” included in the NGEF Statute’s definition of a CIAC is explicitly defined under the NGEF Statute as “a developer of the project *or a person that owns or will own the property served by the project.*”<sup>5</sup> This statutory definition is clear and

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<sup>1</sup> Department Response Comments at 1, 3.

<sup>2</sup> *State v. Rick*, 835 N.W. 2d 478, 482 (Minn. 2013).

<sup>3</sup> Minn. Stat. § 216B.1638, subd. 3(b)(1)-(2).

<sup>4</sup> Department Response Comments at 2.

<sup>5</sup> Minn. Stat. § 216B.1638, subd. 1(c) (emphasis added) (“‘Developer’ means a developer of the project or a person that owns or will own the property served by the project.”). Further, as discussed in MERC’s October 13, 2016, Comments, nothing in the NGEF Statute either requires or prohibits

unambiguous. In this case, the customers who will be served by the proposed Esko Project will be making the CIAC via the monthly NAS charges. There is no basis to argue that those customers are not “person[s] that own[] or will own the property served by the project.” In light of the clear and unambiguous language of the NGEF Statute, the Commission should approve recovery of the proposed Esko Project costs through an NGEF Rider and 25-year NAS, as proposed in MERC’s Initial Filing.

To the extent the Commission believes there is ambiguity regarding the use of the NGEF Rider with an NAS, the legislative history and purpose of the NGEF Statute support a conclusion that the legislature intended the NGEF Rider to be used in combination with an NAS.<sup>6</sup> In accordance with Minn. Stat. § 645.16,

The object of all interpretation and construction of laws is to ascertain and effectuate the intention of the legislature. . . . When the words of a law are not explicit, the intention of the legislature may be ascertained by considering, among other matters: (1) the occasion and necessity for the law; (2) the circumstances under which it was enacted; (3) the mischief to be remedied; (4) the object to be attained; (5) the former law, if any, including other laws upon the same or similar subjects; (6) the consequences of a particular interpretation; (7) the contemporaneous legislative history; and (8) legislative and administrative interpretations of the statute.

MERC provided a detailed discussion in its October 13, 2016, Reply Comments of how the legislative history and objectives of the NGEF Statute support a conclusion that the legislature intended the NGEF Rider to be used in combination with an NAS. Additionally, on October 25, 2016, Representative Pat Garofalo, a chief author of the NGEF Statute, submitted a letter in this docket urging the Commission to approve MERC’s request for NGEF recovery pursuant to Minn. Stat. § 216B.1638 and stating that approval of the Esko Project for NGEF Rider recovery was entirely consistent with the NGEF Statute. According to Representative Garofalo’s letter,

With respect to projects like the Esko and Balaton Projects, which extend natural gas service to previously

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any particular CIAC for a natural gas extension project. Rather, the NGEF Statute merely requires that the utility requesting approval of an NGEF Rider include, in its initial petition, “the amount of any contributions in aid of construction [and] a description of efforts made by the public utility to offset the revenue deficiency through contributions in aid of construction.”

<sup>6</sup> MERC Reply Comments at 2.

unserved areas, the Statute also supports partial recovery of costs through an NGEPRider in combination with a New Area Surcharge. The NGEPRider bill was intended to give utilities an additional tool to use, in combination with the New Area Surcharge mechanism, to make system extensions and expansions affordable where they previously would not have been. In passing the NGEPRider legislation, the Legislature discussed the need for an additional tool to supplement the New Area Surcharge mechanism in order to make extensions to more new areas possible.

This provides further support for a conclusion that the legislature intended the NGEPRider to be used in combination with an NAS.

In its Response Comments, the Department provided little response to MERC's discussion of the legislative history supporting the use of the NGEPRider in combination with an NAS, except to question the significance of a statement made at a March 17, 2015, Minnesota Senate Committee on Environment and Energy hearing. In particular, the Department asserted, "the final statute language appears to be broader than was discussed at the committee hearing (the statute addresses under-served areas as well as expansions) and is silent on whether the NGEPRider can be used in conjunction with the NAS or any other recovery mechanism."<sup>7</sup> But to the extent the final bill was actually broader than the version discussed at the Committee hearing, that would appear to only provide greater support for the conclusion that the NGEPRider Statute was intended to cover a broad variety of circumstances, including being used in concert with the NAS mechanism.

The plain language, legislative intent, and purpose of the NGEPRider and NAS all support approval of MERC's proposal for NGEPRider recovery and a 25-year NAS for the Esko Project.

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<sup>7</sup> Department Response Comments at 2.

## 2. Project Feasibility

Additionally, in its Response Comments, the Department questions MERC's conclusion that the Esko Project would no longer be feasible under the Department's recommendation of a 30-year NAS with no NGEP Rider recovery, asserting that "[t]he Company made no factual comparison to support the argument that the Department's alternative recommendation is not feasible and would deter participation."<sup>8</sup>

As discussed in MERC's October 13, 2016, Reply Comments, MERC conducts significant customer outreach and engages in discussions with relevant local government officials before proceeding with potential new area growth and expansion projects. This outreach includes discussions with prospective customers regarding their interest in conversion to natural gas service, the use of consumer surveys to gauge participation, and an evaluation of alternative fuel costs to develop a reasonable set of assumptions regarding the likely number of customers who would convert at any particular surcharge rate. MERC and its affiliated utilities have significant experience and expertise with expansion projects and the factors that are likely to impact participation.

Additionally, the Company undertakes a thorough evaluation of possible new growth opportunities before determining which opportunities to pursue and under what parameters, and which to reject or postpone for potential future consideration. Such evaluation includes consideration of the relative costs and risks of available growth opportunities. Based on these efforts and analysis, MERC developed its proposal for partial NGEP Rider recovery and a 25-year NAS for the Esko Project. MERC continues to believe the proposed NGEP Rider recovery in conjunction with the 25-year NAS, as set forth in the Company's Initial Filing, is the most reasonable approach to encourage individuals and businesses in the Esko area to participate in the project.

The Department's analysis of an alternative 30-year NAS with no NGEP Rider was based on the assumption that all customers would be converting from propane to natural gas and that the higher NAS charge would not impact the participation rates. Neither of these assumptions is reasonable or supported.

First, with respect to conversion, residents and businesses in the Esko Project area are not all currently served by propane. Based on available information, the majority of customers in this area are not currently served by propane. The following represents the most commonly used home heating fuel sources in Thomson

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<sup>8</sup> Department Response Comments at 3.

Township in Carlton County, which is the closest geographic area near the Esko Project that publishes this data<sup>9</sup>:

Fuel	%
Bottle, Tank, or LP Gas	28%
Electricity	15%
Fuel Oil, Kerosene	47%
Wood	9%
Other	1%

As discussed in MERC’s October 13, 2016, Reply Comments, the cost of conversion to natural gas service will depend on the alternative fuel used, the age of appliances, and other factors. Conversion from fuel oil or wood to natural gas is generally more expensive and often requires installation of a new furnace. Similarly, depending on the system of electric heating, the addition of ductwork can often add significant expense to the conversion. The costs of conversion are an upfront cost that customers consider in determining whether to participate in an NAS project.

Additionally, because a 30-year NAS with no NGEP Rider would result in higher NAS charges, fewer customers would be expected to participate over the life of the Project. As noted in MERC’s October 13, 2016, Comments,

[T]he NAS rates calculated under the Department’s alternative recommendation assume only the term of the NAS changes and holds the remainder of assumptions in the model constant. As a practical matter, MERC would not expect the same participation rate with the charges the Department proposes and the assumptions regarding the number of customers participating in a 30-year NAS would need to be lowered, which would result in even higher surcharges across all customer classes.<sup>10</sup>

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<sup>9</sup> Thomson Township, Carlton County, Minnesota (MN) Detailed Profile, CITY-DATA.COM, <http://www.city-data.com/township/Thomson-Carlton-MN.html> (last visited Nov. 22, 2016).

<sup>10</sup> MERC Reply Comments at 8.

Based on that reality, MERC reran the Esko NAS model with revised participation estimates to reflect the anticipated lower participation levels based on MERC's projection of likely participation at the higher surcharge rates.<sup>11</sup> These adjustments to the expected participation levels result in increases to the monthly NAS charges. In particular, MERC has projected the following updated NAS charges under the Department's proposed 30-year NAS, assuming adjustments to the participation levels to reflect the higher NAS charges:

	<b>MERC Proposed 25-Year NAS/Rider</b>	<b>DOC Recommendation 30-Year NAS/No Rider (updated to reflect anticipated participation)</b>	<b>Difference</b>
Residential	\$24.18	\$38.91	\$14.73
Small C&I	\$45.81	\$73.72	\$27.91
Large C&I	\$114.53	\$184.30	\$69.77
SVI	\$419.95	\$675.78	\$255.83
LVI	\$470.85	\$757.69	\$286.84

The revised NAS model with revised participation assumptions showing the NAS charges under the Department's alternative recommendation is filed separately as Attachment A with these Additional Reply Comments. The nonpublic Attachment A contains trade secret information. Specifically, the cost of plant additions, estimated customer sign-ups, and estimated customer usage contained in Attachment A are not generally known to, and not readily ascertainable by, vendors and competitors of MERC, who could obtain economic value from their disclosure. MERC maintains this information as trade secret. The nonpublic version of Attachment A is filed as a separate Excel file.

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<sup>11</sup> MERC calculated the anticipated change in participation as the percentage that the surcharge would increase under the 30-year NAS with no NGEF. For example, the Residential NAS moved from \$24.18 under MERC's proposal to \$29.21 under a 30-year NAS with no NGEF Rider, assuming no other changes to the participation assumptions. This change equates to a 20.8 percent change in the NAS, which was the percent change applied to the participation assumptions. Changes to the participation rate results in the need for a higher NAS because the total project costs are spread among fewer customers who participate in the project. As the NAS increases, it is expected that fewer customers would choose to participate in the project.

Based on MERC's experience and the relative costs of alternative fuels, it is uncertain whether customers would participate at the levels estimated in Attachment A under the revised surcharges. Ultimately, the Department's alternative proposal is inconsistent with a workable extension project given expected customer participation and other factors. If the Commission adopts the Department's recommendation and only approves the 30-year NAS, MERC would not proceed with the Esko Project and would withdraw the petition in this docket.

MERC continues to request that the Commission approve partial NGEP Rider recovery and a 25-year NAS for the Esko Project, as proposed in MERC's Initial Filing. The record in this docket fully supports a finding that the Esko Project and MERC's proposal for NGEP Rider recovery and 25-year NAS are reasonable and consistent with the public interest.

Please contact me at (651) 322-8965 if you have any questions regarding the information in this filing. Thank you for your attention to this matter.

Sincerely yours,

/s/ Amber S. Lee

Amber S. Lee  
Regulatory and Legislative Affairs Manager  
Minnesota Energy Resources Corporation

cc: Service List



In the Matter of a Petition of Minnesota Energy Resources Corporation for Approval of Recovery of Natural Gas Extension Project Costs through a Rider and a New Area Surcharge for the Esko Project

Docket No. G011/M-16-655

CERTIFICATE OF SERVICE

I, Kristin M. Stastny, hereby certify that on the 23rd of November, 2016, on behalf of Minnesota Energy Resources Corporation (MERC), I electronically filed a true and correct copy of the enclosed Additional Reply Comments on [www.edockets.state.mn.us](http://www.edockets.state.mn.us). Said documents were also served via U.S. mail and electronic service as designated on the attached service list.

Dated this 23rd day of November, 2016.

/s/ Kristin M. Stastny  
Kristin M. Stastny

First Name	Last Name	Email	Company Name	Address	Delivery Method	View Trade Secret	Service List Name
Julia	Anderson	Julia.Anderson@ag.state.mn.us	Office of the Attorney General-DOC	1800 BRM Tower 445 Minnesota St St. Paul, MN 551012134	Electronic Service	Yes	OFF_SL_16-655_M-16-655
Sharon	Ferguson	sharon.ferguson@state.mn.us	Department of Commerce	85 7th Place E Ste 500  Saint Paul, MN 551012198	Electronic Service	No	OFF_SL_16-655_M-16-655
Amber	Lee	ASLee@minnesotaenergyresources.com	Minnesota Energy Resources Corporation	2665 145th St W  Rosemount, MN 55068	Electronic Service	Yes	OFF_SL_16-655_M-16-655
John	Lindell	john.lindell@ag.state.mn.us	Office of the Attorney General-RUD	1400 BRM Tower 445 Minnesota St St. Paul, MN 551012130	Electronic Service	Yes	OFF_SL_16-655_M-16-655
Kristin	Stastny	kstastny@briggs.com	Briggs and Morgan, P.A.	2200 IDS Center 80 South 8th Street Minneapolis, MN 55402	Electronic Service	Yes	OFF_SL_16-655_M-16-655
Daniel P	Wolf	dan.wolf@state.mn.us	Public Utilities Commission	121 7th Place East Suite 350 St. Paul, MN 551012147	Electronic Service	Yes	OFF_SL_16-655_M-16-655

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Minnesota Energy Resources New Area Surcharge Analysis  
 ESKO NEW TOWN GROWTH WITH NNG TAP

Time Period (1)	Year (2)	Net Plant				ADIT		Traditional Revenue Requirements					Retail Revenue (14)	Revenue Excess (Deficy.) (15)	PV of Cash Flows (16)
		Gross Plant Investment (3)	Accumulated Depreciation Reserve (4)	Net Plant In Service (5)	Average Net Plant (6)	Average ADIT (7)	Average Rate Base (8)	Allowed Return (9)	Book Deprec. (10)	O&M Expense (11)	Property Tax (12)	Total Rev. Requir. (13)			
0	2016														
1	2017														
2	2018														
3	2019														
4	2020														
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46	2062														
47	2063														
48	2064														

Reference Page E-2 Page E-2 Page E-2 Page E-2 Page E-2 Calculation Page E-10 Page E-2 Page E-9 x Rate per Customer Page E-2 Calculation Page E-9 Calculation Calculation

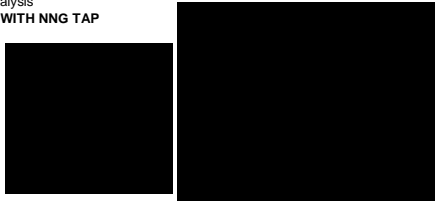
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MERC New Area Surcharge Analysis  
ESKO NEW TOWN GROWTH WITH NNG TAP  
Page E-2

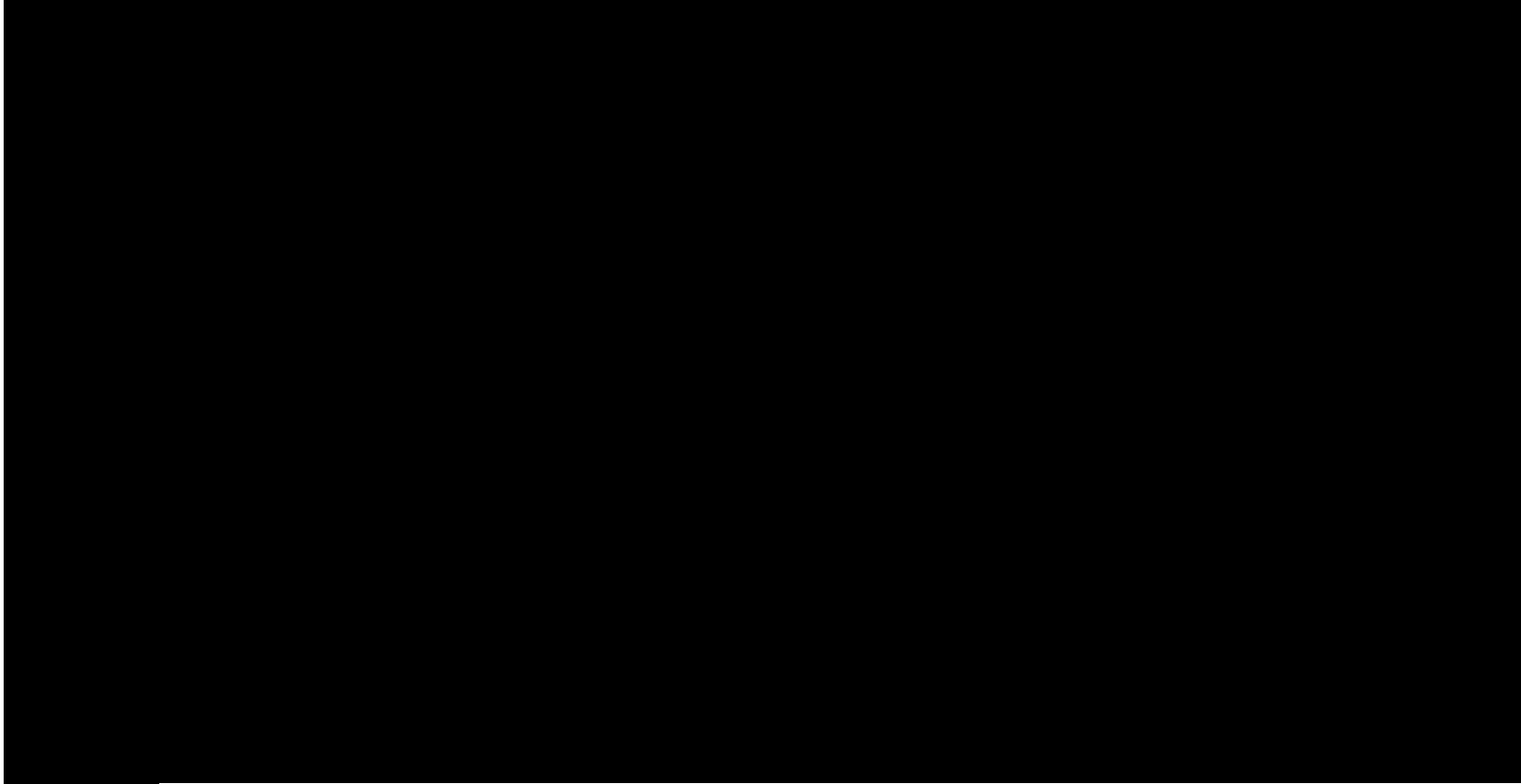
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Total CIAC  
Total Net Investment

Book Depreciation Rate

Tax Rate



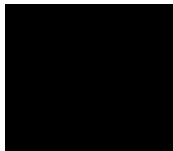
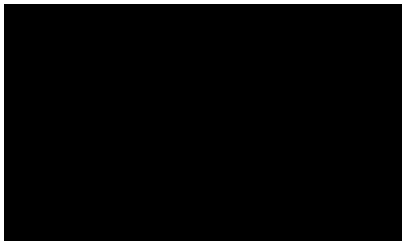
Net Plant					ADIT - Property					ADIT - Surcharge Revenues					Total ADIT	Property Taxes
Gross Plant	Depreciation	Accum. Res.	Net Plant	Avg Net Plant	Tax Rates	Tax Deprec.	Cum Tax Deprec.	Book-Tax Deprec.	Acc. Def. Tax	Avg. ADIT	Annual Surcharge Revenue	CIAC	Tax	Cum Tax	Avg ADIT	



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MERC New Area Surcharge Analysis  
ESKO NEW TOWN GROWTH WITH NNG TAP  
Page E-3

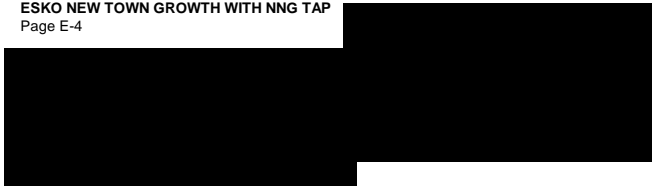


Year	Net Plant			ADIT - Property				
	Gross Plant	Depreciation	Acum. Res.	Net Plant	Avg Net Plant	Tax Rates	Tax Deprec.	Cum. Tax Deprec.
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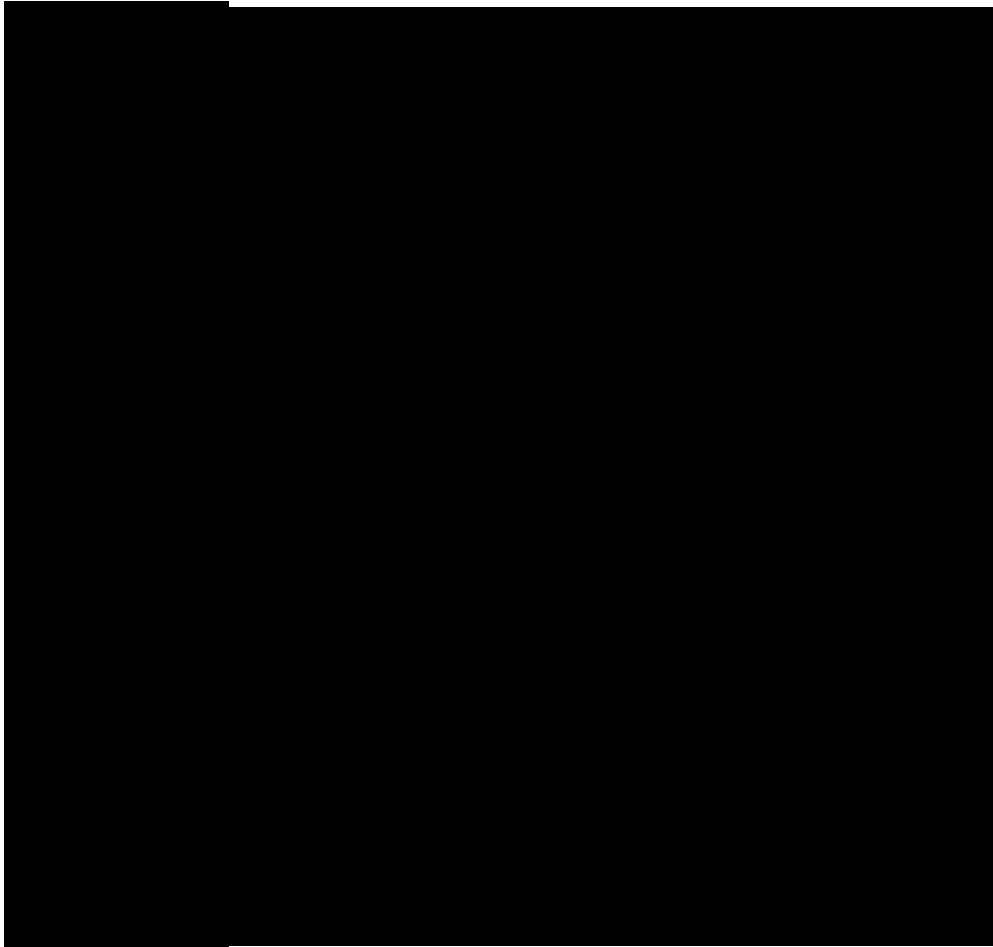
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MERC New Area Surcharge Analysis  
ESKO NEW TOWN GROWTH WITH NNG TAP  
Page E-4



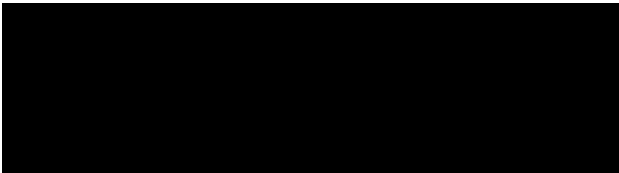
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	Gross Plant	Depreciation	Accum. Res.					Cum Tax Deprec.



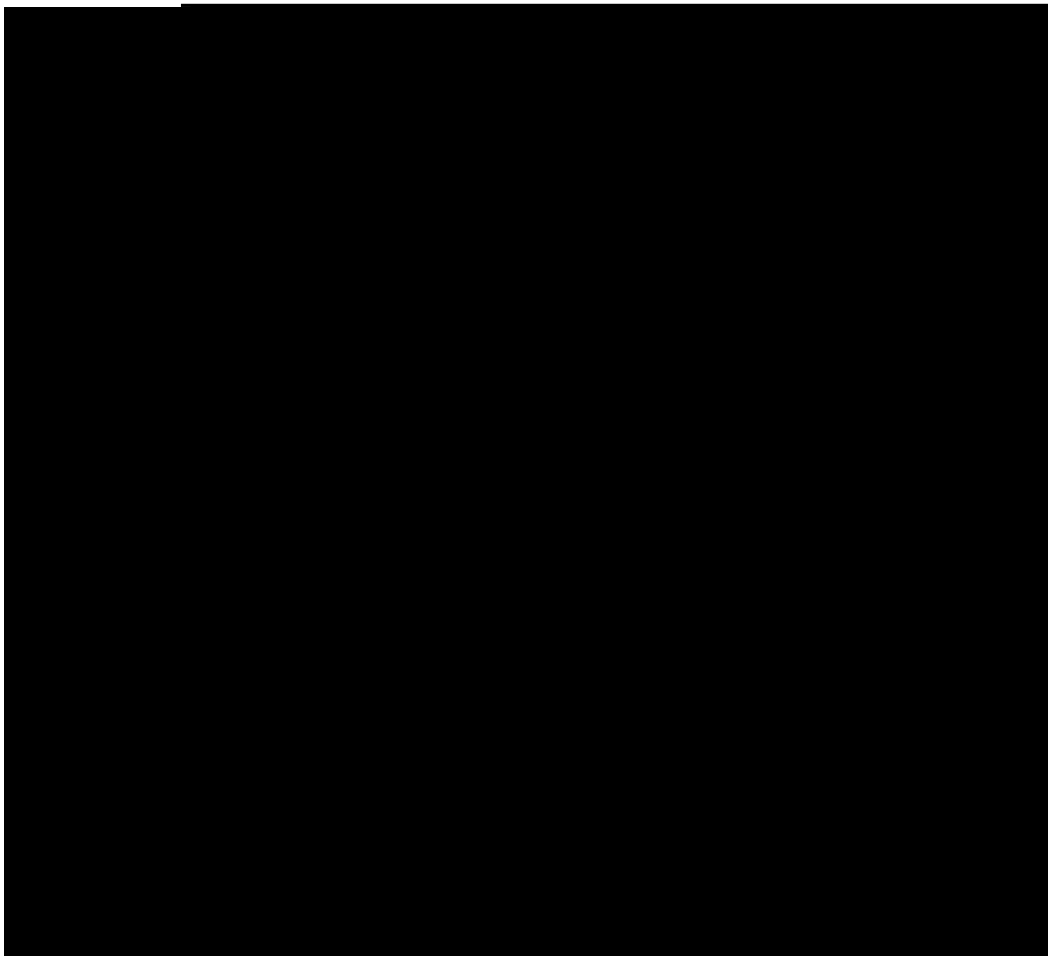
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MERC New Area Surcharge Analysis  
ESKO NEW TOWN GROWTH WITH NNG TAP



Year	Net Plant			Net Plant	Avg Net Plant	Tax Rates	Tax Deprec.	ADIT - Prop
	Gross Plant	Depreciation	Accum. Res.					Cum Tax Deprec.



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MERC New Area Surcharge Analysis  
ESKO NEW TOWN GROWTH WITH NNG TAP  
Page E-6



Year	Gross		Net Plant			Tax	Tax	ADIT - Prop
	Plant	Depreciation	Accum. Res.	Plant	Avg Net Plant	Rates	Deprec.	Cum Tax Deprec.

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MERC New Area Surcharge Analysis  
ESKO NEW TOWN GROWTH WITH NNG TAP  
Page E-7

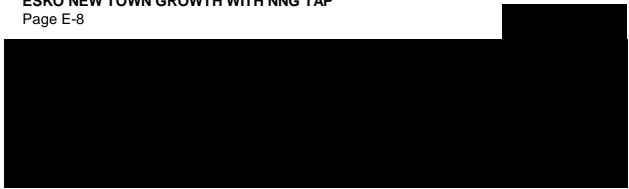


Year	Net Plant			Net Plant	Avg Net Plant	Tax Rates	Tax Deprec.	ADIT - Prop
	Gross Plant	Depreciation	Accum. Res.					Cum Tax Deprec.
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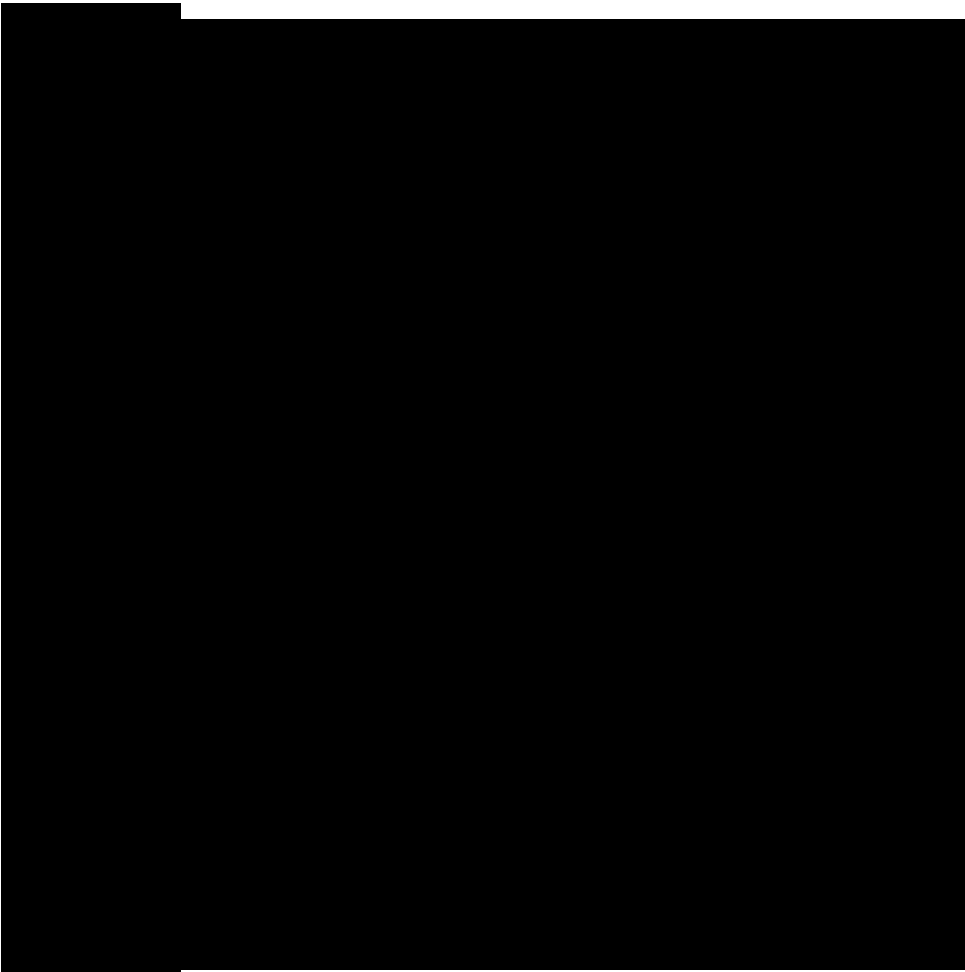
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MERC New Area Surcharge Analysis  
ESKO NEW TOWN GROWTH WITH NNG TAP  
Page E-8



Year	Gross Plant		Net Plant		Tax		ADIT - Prop
	Plant	Depreciation	Accum. Res.	Plant	Avg Net Plant	Rates	Tax Deprec.



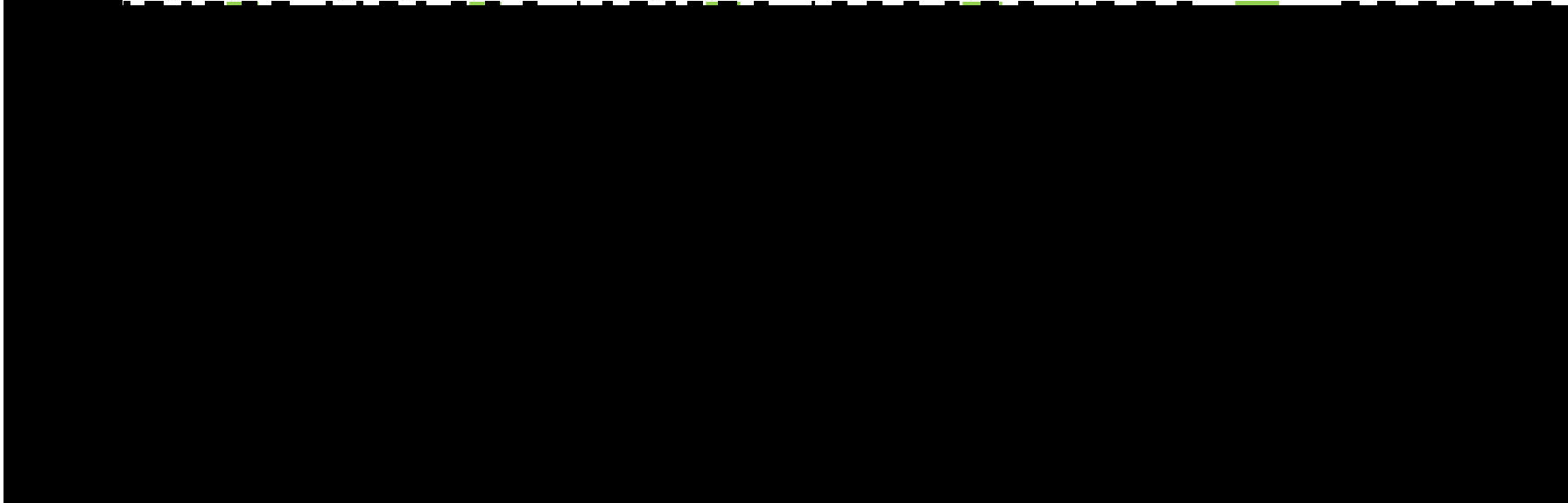
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ESKO NEW TOWN GROWTH WITH NNG TAP

Year	Residential						Commercial - Small						Commercial - Large						Small Volume Interruptible						Large Volume Interruptible						Summary		Surcharge Info			
	Average Customers	Annual Throughput / Customer	Volume/Margin / Unit	Small Base Charge / Customer	Annual Retail Revenue	Monthly Surcharge Per Customer	Average Customers	Annual Throughput / Customer	Volume/Margin / Unit	Small Base Charge / Customer	Annual Retail Revenue	Monthly Surcharge Per Customer	Average Customers	Annual Throughput / Customer	Volume/Margin / Unit	Small Base Charge / Customer	Annual Retail Revenue	Monthly Surcharge Per Customer	Average Customers	Annual Throughput / Customer	Volume/Margin / Unit	Small Base Charge / Customer	Annual Retail Revenue	Monthly Surcharge Per Customer	Total Customers	Total Retail Revenue	Total Surcharge Recover	Tax G-Up on Surcharge	Capex Total Surcharge Recover	Opex Total Surcharge Recover						

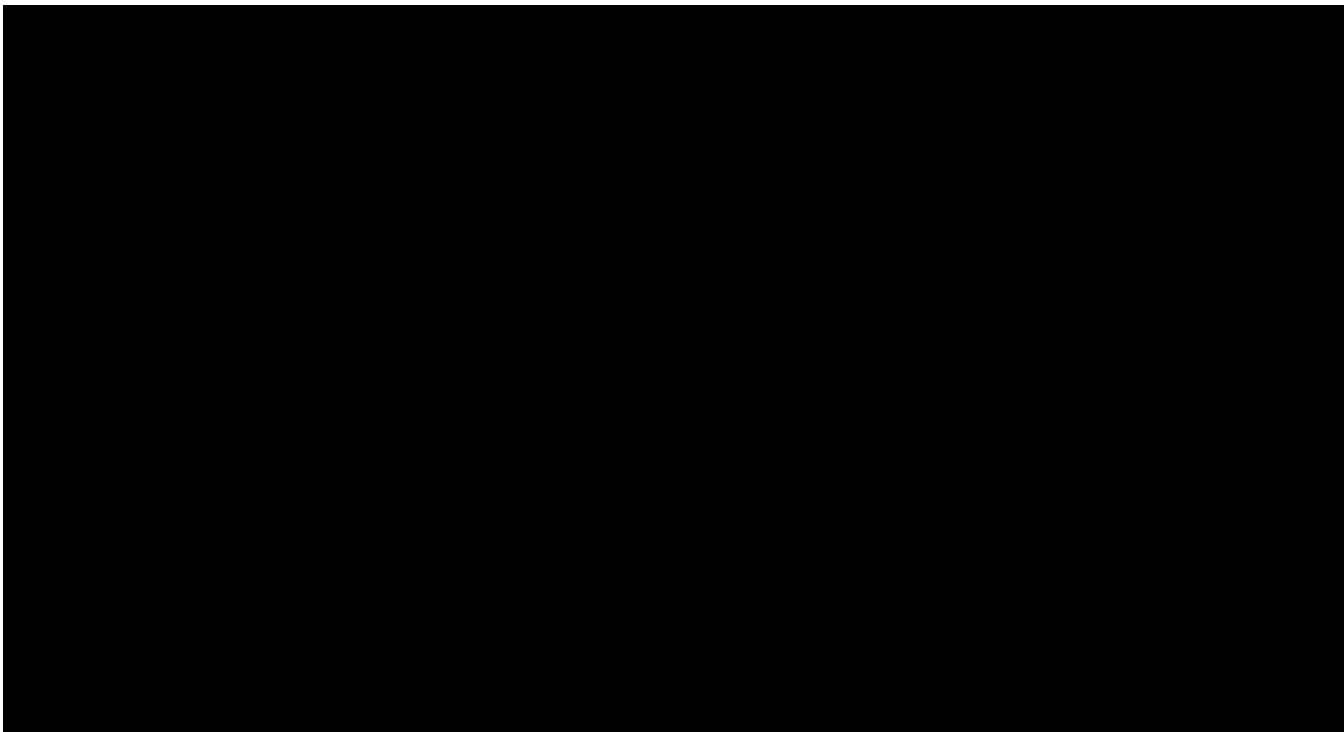


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MERC New Area Surcharge Analysis  
**ESKO NEW TOWN GROWTH WITH NNG TAP**  
Page E-10

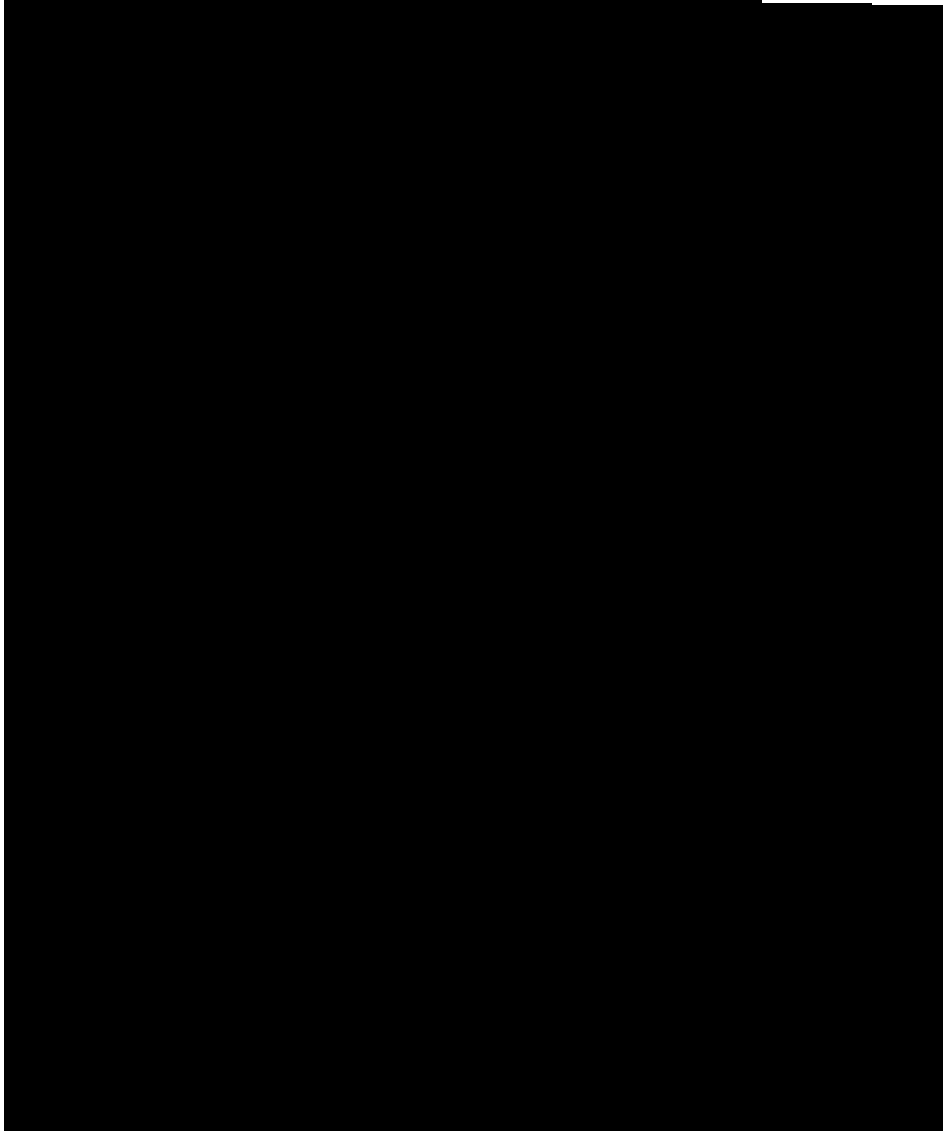
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**ESKO NEW TOWN GROWTH WITH NNG TAP**

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**ESKO NEW TOWN GROWTH WITH NNG TAP**

Assumptions

Construction Costs (infrastructure)  
CIAC

**Customer's Sign-Up**

**Annual Throughput**

**Total Project  
Less Tap Cost  
Subtotal**

Capital Cost after Socialization

Tap Cost

Tap Cost after Socialization

**Total Socialization**

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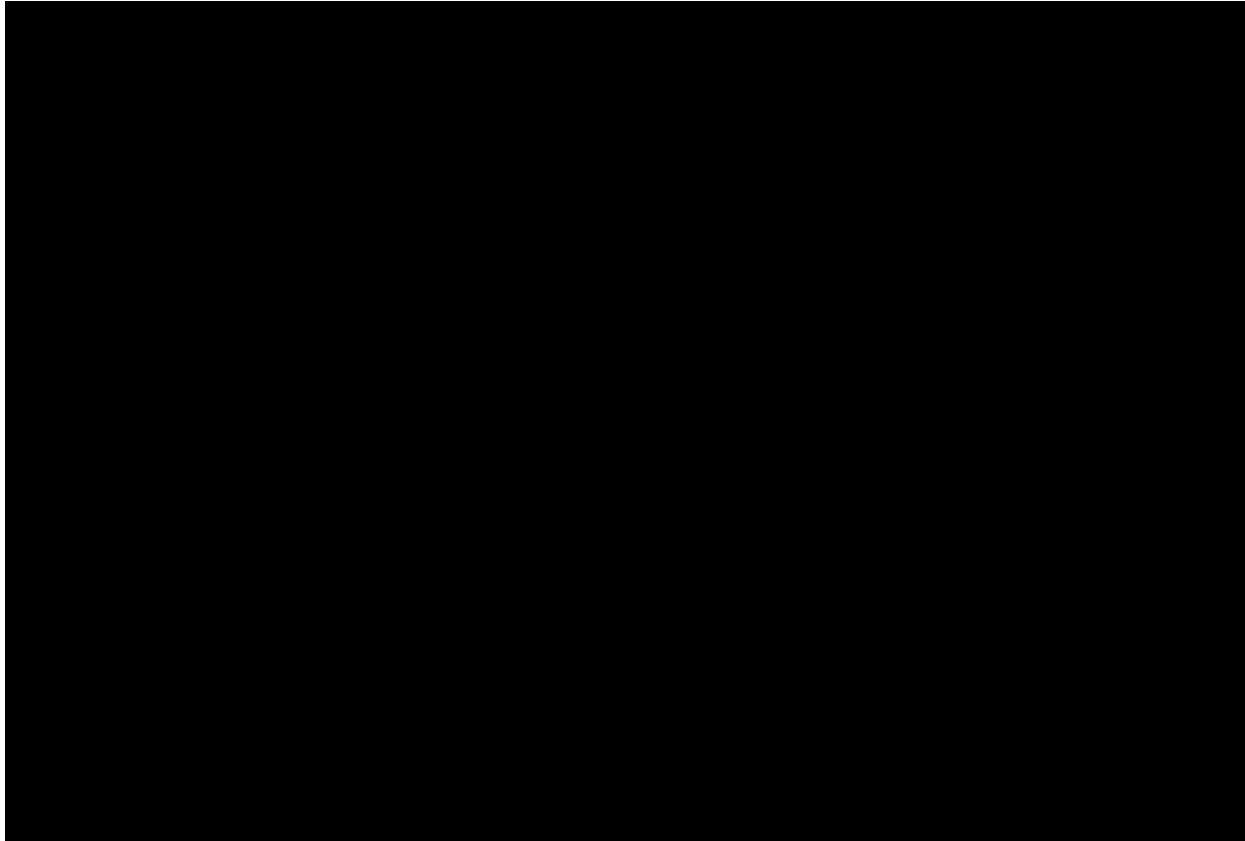
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**Esko Tap Cost Amortization Schedule**

Tap Cost: █ █

Year	Beg Balance (excl carry cost)	Annual Amortization	Balance (excl carry Cost)	Annual Carry Cost	Annual O&M Expense (Amortization and Carry Cost)
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**NGEP Rider Calculation**

Total Costs Proposed for Recovery in NGEP Rider

Sales Forecast approved in GR-13-617

Rider Calculation



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